

LABARGE INC
Form 10-Q
November 05, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934
For the quarterly period ended October 3, 2010

or

Transition Report Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission File Number: 1-5761

LaBarge, Inc.

(Exact name of registrant as specified in its charter)

Delaware

73-0574586

(State or Other Jurisdiction of
Incorporation or Organization)

(I.R.S. Employer Identification Number)

9900 Clayton Road, St. Louis, Missouri

63124

(Address of Principal Executive Offices)

(Zip Code)

(314) 997-0800

(Registrant's Telephone Number, Including Area Code)

N/A

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

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Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the Issuer's classes of common stock as of November 4, 2010: 15,808,331 shares of common stock.

LaBarge, Inc.

FORM 10-Q

For the Quarterly Period Ended October 3, 2010

Table of Contents

Part I

Financial Information

Item 1.

Financial Statements.

Consolidated Statements of Income
Consolidated Balance Sheets
Consolidated Statements of Cash
Flows
Notes to Consolidated Financial
Statements

Item 2.

Management's Discussion and Analysis of Financial
Condition and Results of Operations.

Item 3.

Quantitative and Qualitative Disclosures About Market
Risk.

Item 4.

Controls and Procedures.

Part II

Other Information

Item 1A.

Risk Factors.

Item 6.

Exhibits.

Signature

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

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LaBARGE, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(amounts in thousands, except per-share amounts)

	Three Months Ended	
	October 3, 2010	September 27, 2009
Net sales	\$ 85,448	\$ 63,155
Cost of sales	68,017	50,925
Gross profit	17,431	12,230
Selling and administrative expense	9,401	8,090
Operating income	8,030	4,140
Interest expense	398	508
Other (income) expense, net	(6)	24
Earnings before income taxes	7,638	3,608
Income tax expense	2,710	505
Net earnings	\$ 4,928	\$ 3,103
Basic net earnings per common share	\$ 0.31	\$ 0.20
Average basic common shares outstanding	15,685	15,743
Diluted net earnings per common share	\$ 0.31	\$ 0.19
Average diluted common shares outstanding	15,898	16,048

See accompanying Notes to Consolidated Financial Statements.

LaBARGE, INC.
CONSOLIDATED BALANCE SHEETS
(Unaudited)

(amounts in thousands, except per-share amounts)

	October 3, 2010	June 27, 2010
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ASSETS**Current assets:**

Cash and cash equivalents	\$	235	\$	2,301
Accounts and other receivables, net		45,039		46,807
Inventories		72,103		64,536
Prepaid expenses		1,538		1,062
Deferred tax assets, net		3,805		3,655
Total current assets		122,720		118,361
Property, plant and equipment, net of accumulated depreciation of \$37,191 at October 3, 2010, and \$35,704 at June 27, 2010		27,552		28,536
Intangible assets, net		8,540		9,076
Goodwill		43,424		43,424
Other assets		5,199		5,125
Total assets	\$	207,435	\$	204,522

LIABILITIES AND STOCKHOLDERS' EQUITY**Current liabilities:**

Short-term borrowings	\$	550	\$	---
Current maturities of long-term debt		10,231		12,069
Trade accounts payable		27,834		26,538
Accrued employee compensation		12,168		14,625
Other accrued liabilities		6,148		3,712
Cash advances from customers		3,423		2,921
Total current liabilities		60,354		59,865
Long-term advances from customers for purchase of materials		308		46
Deferred tax liabilities, net		2,494		2,494
Deferred gain on sale of real estate and other liabilities		1,127		1,219
Long-term debt		22,554		25,258

Stockholders' equity:

Common stock, \$0.01 par value. Authorized 40,000,000 shares; 15,958,839 issued at both October 3, 2010, and June 27, 2010, including shares in treasury		160		160
Additional paid-in capital		13,799		14,582
Retained earnings		108,755		103,827
Accumulated other comprehensive loss		(250)		(222)
Less cost of common stock in treasury shares of 160,008 at October 3, 2010, and 234,651 at June 27, 2010		(1,866)		(2,707)
Total stockholders' equity		120,598		115,640
Total liabilities and stockholders' equity	\$	207,435	\$	204,522

See accompanying Notes to Consolidated Financial Statements.

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(amounts in thousands)

	Three Months Ended	
	October 3, 2010	September 27, 2009
Cash flows from operating activities:		
Net earnings	\$ 4,928	\$ 3,103
Adjustments to reconcile net cash provided by operating activities:		
Loss on disposal of property, plant and equipment	---	14
Depreciation and amortization	2,168	2,238
Amortization of deferred gain on sale of real estate	(120)	(120)
Share-based compensation	376	308
Deferred taxes	(148)	(78)
Changes in operating assets and liabilities:		
Accounts and other receivables, net	1,768	(478)
Inventories	(7,567)	(660)
Prepaid expenses	(476)	(167)
Trade accounts payable	1,132	2,563
Accrued liabilities	212	1,422
Cash advances from customers	764	(1,883)
Net cash provided by operating activities	3,037	6,262
Cash flows from investing activities:		
Additions to property, plant and equipment	(401)	(1,922)
Proceeds from disposal of property, equipment and other assets	4	13
Additions to other assets	(161)	(287)
Net cash used by investing activities	(558)	(2,196)
Cash flows from financing activities:		
Borrowings on revolving credit facility	9,075	---
Payments of revolving credit facility	(8,525)	---
Repayments of long-term debt	(4,542)	(40)
Excess tax benefits from stock option exercises	---	387
Remittance of minimum taxes withheld as part of a net share settlement of stock option exercises	(562)	(841)
Issuance of treasury stock	9	63
Purchase of treasury stock	---	(140)
Net cash used by financing activities	(4,545)	(571)
Net (decrease) increase in cash and cash equivalents	(2,066)	3,495
Cash and cash equivalents at beginning of period	2,301	4,297
Cash and cash equivalents at end of period	\$ 235	\$ 7,792

See accompanying Notes to Consolidated Financial Statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated balance sheets at October 3, 2010, and the related consolidated statements of income and cash flows for the three months ended October 3, 2010 and September 27, 2009, have been prepared by LaBarge, Inc. (the "Company") without audit. In the opinion of management, adjustments, all of a normal and recurring nature, necessary to present fairly the financial position and the results of operations and cash flows for the aforementioned periods, have been made. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions in certain circumstances that affect amounts reported in the accompanying consolidated financial statements. In preparing these financial statements, management has made its best estimates and judgment of certain amounts included in the financial statements. Areas involving significant judgments and estimates include revenue recognition and cost of sales, inventories, and goodwill and intangible assets. Actual results could differ from those estimates.

Certain items in the prior year's consolidated financial statements have been reclassified to conform to the current year presentation. For the three months ended September 27, 2009, the Company revised its presentation of cash flows from the purchase of treasury stock, the issuance of treasury stock and the remittance of minimum taxes withheld as a part of net settlements of share-based payments. The total net cash flow provided by financing activities did not change nor did this impact any other presented financial information. The impact of the revision was not considered material to the previously issued financial statements.

During the first quarter of fiscal year 2010, the Company recorded a \$795,000 reduction to income tax expense from a correction in the apportionment factor for state income tax returns for fiscal years 2006 through 2009 and an increase in other tax expense, included in selling and administrative expense, of \$193,000 (\$125,000 after-tax) for a gross receipts tax that relates to fiscal years 2005 through 2009. The \$795,000 reduction to income tax expense is net of the federal income taxes. The Company determined that the amounts that related to prior fiscal years were not material to any of the respective prior fiscal years, therefore, recognized the adjustments during the first quarter of fiscal year 2010. The net impact of both adjustments to net earnings was an increase of \$670,000 for the three months ended September 27, 2009, which had a \$0.04 impact on basic and diluted earnings per share. The impact on full-year net earnings for fiscal year 2010 was not material.

Recently Adopted Accounting Standards

In June 2009, the Financial Accounting Standards Board ("FASB") issued an accounting standards update included in Accounting Standards Codification ("ASC") Topic 810, "Consolidation," which amends previous guidance to require an analysis to determine whether a variable interest gives a company a controlling financial interest in a variable interest entity. An ongoing reassessment of financial responsibility is required, including interests in entities formed prior to the effective date of this guidance. This guidance also eliminates the quantitative approach previously required for determining whether a company is the primary beneficiary. It is effective for fiscal years beginning after November 15, 2009. This guidance was adopted by the Company on June 28, 2010, and adoption did not have a material impact on the Company's consolidated financial statements.

In October 2009, the FASB issued guidance titled "Revenue Recognition – Multiple Deliverable Revenue Arrangements" (Accounting Standards Update 2009-13), which requires entities to allocate revenue in an arrangement using estimated selling prices of the delivered goods and services based on a selling price hierarchy. The guidance eliminates the residual method of revenue allocation and requires revenue to be allocated using the relative selling price method. This guidance should be applied on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. This guidance was adopted on June 28, 2010, and adoption did not have a material impact on the Company's consolidated financial statements.

2. SALES AND NET SALES

Sales and net sales consist of the following:

(in thousands)

	Three Months Ended	
	October 3, 2010	September 27, 2009
Sales	\$ 85,562	\$ 63,294
Less sales discounts	114	139

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Net sales	\$	85,448	\$	63,155
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Geographic Information

The Company has no sales offices or facilities outside of the United States. Sales for exports were 10.9% of total sales for the fiscal quarter ended October 3, 2010. The exports exceeded 10% of total sales due to a large contract related to wind power generation equipment. This contract is denominated in U.S. dollars and, therefore, the Company does not have foreign currency risk associated with the related accounts receivable.

Customer Information

The Company's top three customers and their relative contributions to sales for the three months ended October 3, 2010, were as follows: Owens-Illinois, Inc., \$13.4 million (15.6%); American Superconductor, \$8.7 million (10.1%); and Schlumberger, Ltd., \$7.7 million (9.0%). This compares with Owens-Illinois, Inc., \$6.9 million (10.9%); BAE Systems, \$5.8 million (9.2%); and Raytheon Company, \$5.4 million (8.6%) for the three months ended September 27, 2009.

3. ACCOUNTS AND OTHER RECEIVABLES

Accounts and other receivables consist of the following:

(in thousands)

	October 3, 2010	June 27, 2010
Billed shipments	\$ 44,944	\$ 46,890
Less allowance for doubtful accounts	267	285
Trade receivables, net	44,677	46,605
Other current receivables	362	202
Total	\$ 45,039	\$ 46,807

Included in accounts receivable at October 3, 2010, and June 27, 2010, were \$138,000 and \$407,000, respectively, of receivables due directly from the U.S. Government and \$15.1 million and \$14.8 million, respectively, due from customers related to contracts with the U.S. Government.

At October 3, 2010, the amounts due from the three largest accounts receivable debtors and the percentage of total accounts receivable represented by those amounts were \$10.2 million (22.8%), \$6.0 million (13.3%), and \$3.1 million (6.9%). This compares with \$10.1 million (21.5%), \$6.6 million (14.0%), and \$3.4 million (7.2%) at June 27, 2010.

4. INVENTORIES

Inventories consist of the following:

(in thousands)

	October 3, 2010	June 27, 2010
Raw materials	\$ 47,042	\$ 42,602
Work in progress	7,151	4,658

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Inventoried costs relating to long-term contracts, net of amounts attributable to revenues recognized to date	12,914	13,399
Finished goods	4,996	3,877
Total	\$ 72,103	\$64,536

For the three months ended October 3, 2010, and September 27, 2009, expense for obsolete or slow-moving inventory charged to income before taxes was \$472,000 and \$255,000, respectively.

The following table shows the cost elements included in the inventoried costs related to long-term contracts:

(in thousands)

	October 3, 2010	June 27, 2010
Production costs of goods currently in process ⁽¹⁾	\$ 12,231	\$ 13,054
Excess of production costs of delivered units over the estimated average cost of all units expected to be produced, including tooling and non-recurring costs	892	642
Unrecovered costs subject to future negotiation	47	---
Reserve for contracts with estimated costs in excess of contract revenues	(256)	(297)
Total inventoried costs	\$ 12,914	\$ 13,399

(1) Selling and administrative expenses are not included in inventory costs.

Deferred production costs generally tend to be significant on large multi-year contracts for which the Company has not previously produced the product.

The inventoried costs relating to long-term contracts include unrecovered costs of \$47,000 and \$0 at October 3, 2010, and June 27, 2010, respectively, which are subject to future determination through negotiation or other procedures not complete at October 3, 2010. In the opinion of management, these costs will be recovered by contract modification.

The Company records a loss when the estimated costs of a contract exceed the net realizable value of contract. The Company has recorded a provision equal to the amount that estimated costs would exceed the net realizable revenue over the contract.

5. INTANGIBLE ASSETS, NET

Intangible assets, net, consist of the following:

(in thousands)

	October 3, 2010	June 27, 2010
Software	\$ 5,478	\$5,446
Less accumulated amortization	4,547	4,432
Net software	931	1,014
Customer lists	9,670	9,670
Less accumulated amortization	2,162	1,836
Net customer lists	7,508	7,834
Employee agreements	950	950
Less accumulated amortization	849	722

Total inventoried costs

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Net employee agreements	101	228
Total	\$ 8,540	\$9,076

Intangible assets are amortized over a period ranging from two to eight years. Amortization expense was \$598,000 for the three months ended October 3, 2010, compared with \$707,000 for the three months ended September 27, 2009.

The Company anticipates that amortization expense will approximate \$2.1 million for fiscal year 2011, \$1.9 million for fiscal year 2012, \$1.7 million for fiscal year 2013, \$1.6 million for fiscal year 2014, and \$1.6 million for fiscal year 2015.

The Company assesses the assets for impairment in accordance with ASC 360-10, Property, Plant, and Equipment – Impairment of Disposal of Long-Lived Assets. Impairment is realized when the undiscounted cash flows to be derived from the asset are less than its carrying amount. If impairment exists, the carrying value of the impaired asset is reduced to its net realizable value. The impairment charge is recorded in operating results. There was no impairment charge during the three months ended October 3, 2010, or during fiscal year 2010.

6. GOODWILL

Goodwill is summarized as follows:

(in thousands)

	October 3, 2010	June 27, 2010
Goodwill	\$ 43,424	\$43,424

Goodwill is recorded at three of the Company's reporting units. Impairment is tested annually in the fourth quarter of each fiscal year or more frequently if events or circumstances warrant.

7. OTHER ASSETS

Other assets consist of the following:

(in thousands)

	October 3, 2010	June 27, 2010
Cash value of life insurance	\$ 4,819	\$4,723
Deposits and licenses	177	186
Deferred financing costs, net	116	141
Other	87	75
Total	\$ 5,199	\$5,125

The cash value of life insurance relates to Company-owned life insurance policies on certain current and retired key employees.

8. SHORT- AND LONG-TERM OBLIGATIONS

Short-term borrowings, long-term debt and current maturities of long-term debt consist of the following:

(dollars in thousands)

October 3,	June 27,
---------------	----------

Total inventoried costs

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	2010	2010
Short-term borrowings:		
Revolving credit agreement:		
Balance at period-end	\$ 550	\$ ---
Interest rate at period-end	3.75%	3.75%
Average amount of short-term borrowings outstanding during period	\$ 183	\$ 35
Average interest rate for period	3.79%	3.79%
Maximum short-term borrowings at any month-end	\$ 550	\$ ---
Senior long-term debt:		
Term loan	\$ 32,500	\$ 37,000
Other	285	327
Total senior long-term debt	32,785	37,327
Less current maturities	10,231	12,069
Long-term debt, less current maturities	\$ 22,554	\$ 25,258

The average interest rate was computed by dividing the sum of daily interest costs by the sum of the daily borrowings for the respective periods.

Senior Lender:

The Company entered into a senior secured loan agreement on December 22, 2008, amended on January 30, 2009. The following is a summary of certain provisions of the agreement:

- The agreement provides for a revolving credit facility, of up to \$30.0 million, which is available for direct borrowings or letters of credit. The facility is based on a borrowing base formula equal to the sum of 85% of eligible receivables and 35% of eligible inventories. As of October 3, 2010, \$550,000 was outstanding under the revolving credit facility. As of October 3, 2010, letters of credit issued were \$1.2 million, leaving an aggregate of up to \$28.2 million available under the revolving credit facility. This credit facility matures on December 22, 2011.
- The agreement provides for an aggregate \$45.0 million term loan, with quarterly principal payments beginning in September 2009 of \$2.0 million, increasing to \$2.5 million in September 2010 and increasing to \$2.7 million in September 2011. The balance is due on December 22, 2011.
- Interest on the revolving facility and the term loan is calculated at a base rate or LIBOR plus a stated spread based on certain ratios. For the fiscal quarter ended October 3, 2010, the average rate was approximately 3.61%.
- All loans are secured by substantially all the assets of the Company other than real estate.
- The Company must comply with covenants and certain financial performance criteria consisting of Earnings Before Interest, Taxes, Depreciation and Amortization in relation to debt, minimum net worth and operating cash flow in relation to fixed charges. The Company was in compliance with its borrowing agreement covenants as of and during the fiscal quarter ended October 3, 2010.

Interest Rate Swap:

To mitigate the risk associated with interest rate volatility, the Company entered into an interest rate swap agreement. This pay-fixed, receive-floating rate swap limits the Company's exposure to interest rate variability and allows for better cash flow control. The swap is not used for speculative purposes.

Under the original agreement, the Company fixed the interest payments to a base rate of 1.89% plus a stated spread based on certain ratios. The beginning notional amount is \$35.0 million, which will amortize simultaneously with the term loan schedule in the associated loan agreement and will mature on December 22, 2011. At October 3, 2010, the outstanding balance under the associated loan agreement was \$25.3 million.

On September 30, 2009, the Company made an additional payment in conjunction with the first principal payment under the loan agreement dated December 22, 2008. This additional payment, reflected in the financial statements as a current maturity of long-term debt in addition to the contractual payments due within the next twelve months, required a restructuring of the interest rate swap agreement. As a result, the fixed

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base rate under the revised agreement increased to 1.92%. This rate will apply until the swap matures on December 22, 2011.

The interest rate swap agreement has been designated as a cash flow hedging instrument, and the Company has formally documented, designated and assessed the effectiveness of the interest rate swap. The financial statement impact of ineffectiveness for the three months ended October 3, 2010, and September 27, 2009, was immaterial.

Fair Value:

The Company considered the carrying amounts of cash and cash equivalents, securities and other current assets and liabilities, including accounts receivable and accounts payable, to approximate fair value because of the short maturity of these financial instruments.

The Company has considered amounts outstanding under the long-term debt agreements and determined that carrying amounts recorded in the financial statements are consistent with the estimated fair value as of October 3, 2010.

Additionally, the interest rate swap agreement, further described above, has been recorded by the Company based on the estimated fair value as of October 3, 2010.

At October 3, 2010, the Company recorded a liability of \$390,000 classified within other long-term liabilities in the consolidated balance sheet, and accumulated other comprehensive loss of \$250,000 (net of deferred income tax effects of \$140,000) relating to the fair value of the interest rate swap contract.

The Company has classified its financial assets and liabilities using a three-level hierarchy for disclosure of fair value measurements, based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date, as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 – inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Company's interest rate swap is valued using a present value calculation based on an implied forward LIBOR curve (adjusted for the Company's credit risk) and is classified within Level 2 of the valuation hierarchy, as presented below:

(in thousands)

	Fair Value as of October 3, 2010			
	Level 1	Level 2	Level 3	Total
Other long-term liabilities:				
Interest rate swap derivative	\$ ---	\$ 390	\$ ---	\$ 390
	\$ ---	\$ 390	\$ ---	\$ 390

Other Long-Term Debt:

Other long-term debt includes capital lease agreements with outstanding balances totaling \$35,000 at October 3, 2010, and \$77,000 at June 27, 2010.

Maturities of Senior Long-Term Debt:

The aggregate maturities of long-term obligations are as follows:

Total inventoried costs

(in thousands)

Fiscal Year	
2011	\$ 7,527
2012	25,258
Total	\$32,785

9. CASH FLOWS

Total cash payments for interest for the three months ended October 3, 2010, and September 27, 2009 amounted to \$828,000 and \$475,000, respectively. Net cash payments for federal and state income taxes were \$373,000 and \$15,000 for the three months ended October 3, 2010, and September 27, 2009, respectively.

10. COMPREHENSIVE INCOME

Comprehensive income consists of the following:

(in thousands)

	Three Months Ended	
	October 3, 2010	September 27, 2009
Net income	\$4,928	\$ 3,103
Other comprehensive loss	28	73
Comprehensive income	\$4,900	\$ 3,030

The other comprehensive loss of \$28,000 recognized in the three months ended October 3, 2010, represents the result of the changes in the fair value of the interest rate swap agreement described in note 8. The agreement has been designated as a hedge of the variability of cash flows associated with the floating rate debt and has met current effectiveness criteria.

11. EARNINGS PER COMMON SHARE

Basic and diluted earnings per common share are computed as follows:

(amounts in thousands, except earnings per-share amounts)

	Three Months Ended	
	October 3, 2010	September 27, 2009
Net earnings	4,928	\$ 3,103
Basic net earnings per common share	0.31	\$ 0.20
Diluted net earnings per	0.31	\$ 0.19

Total inventoried costs

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common
share

Basic earnings per share are calculated using the weighted-average number of common shares outstanding during the period. Diluted earnings per share are calculated under the treasury stock method using the weighted-average number of common shares outstanding during the period plus shares issuable upon the assumed exercise of dilutive common share options.

Basic and diluted shares are computed as follows:

(in thousands)

	Three Months Ended	
	October 3, 2010	September 27, 2009
Average common shares outstanding – basic	15,685	15,743
Dilutive options and nonvested shares	213	305
Adjusted average common shares outstanding – diluted	15,898	16,048

All stock options outstanding and nonvested shares at October 3, 2010, and September 27, 2009 were dilutive and included in the computation of diluted earnings per share. These options expire in various periods through 2014. The Company had awarded certain key executives nonvested shares tied to the Company's fiscal year 2010 financial performance. The compensation expense related to these awards is recognized quarterly. The nonvested shares vest at the end of the fiscal year 2012.

12. STOCK-BASED ARRANGEMENTS

The Company has established the 1993 Incentive Stock Option Plan, the 1995 Incentive Stock Option Plan and the 1999 Non-Qualified Stock Option Plan (collectively, the "Plans"). The Plans provide for the issuance of up to 2.2 million shares to be granted in the form of share-based awards to key employees of the Company. In addition, pursuant to the 2004 Long Term Incentive Plan ("LTIP"), the Company provides for the issuance of up to 850,000 shares to be granted in the form of share-based awards to certain key employees and nonemployee directors. The Company may satisfy the awards upon exercise with either new or treasury shares. The Company's share-based compensation awards outstanding at October 3, 2010, include stock options, restricted stock and performance units.

For the three months ended October 3, 2010, total share-based compensation was \$376,000 (\$241,000 after-tax), equivalent to earnings per basic and diluted shares of \$0.02. For the three months ended September 27, 2009, total share-based compensation was \$308,000 (\$196,000 after-tax), equivalent to earnings per basic and diluted shares of \$0.01.

As of October 3, 2010, the total unrecognized compensation expense related to nonvested shares and performance units was \$856,000 before income tax, and the period over which it is expected to be recognized is approximately two years. At September 27, 2009, the total unrecognized compensation expense related to nonvested shares and performance units was \$461,000 before income tax, and the period over which it was recognized was approximately one year.

Stock Options

A summary of the activity in the Company's Plans during the three months ended October 3, 2010, is presented below:

	Number of Shares	Weighted- Average Exercise Price	Number of Shares Exercisable	Weighted- Average Exercise Price	Weighted- Average Fair Value of Granted Options
Outstanding at June 27, 2010	426,652	\$ 5.61	426,652	\$ 5.61	

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Exercised	1,000	8.54	---	---	---
Outstanding at October 3, 2010	425,652	\$ 5.60	425,652	\$ 5.60	

The following table summarizes information about stock options outstanding and exercisable as of October 3, 2010:

Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life (In Years)	Weighted-Average Exercise Price	Aggregate Intrinsic Value (1) (in millions)
\$2.50 – 3.00	112,900	0.9	\$ 2.85	\$ 1.1
\$3.01 – 5.96	121,600	2.8	3.53	1.1
\$5.97 – 8.54	191,152	3.9	8.54	0.8
	425,652	2.8	\$ 5.60	\$ 3.0

The intrinsic value of a stock option is the amount by which the October 3, 2010, market value of the underlying stock exceeds the exercise price of the option.

The total intrinsic value of stock options exercised during the fiscal quarters ended October 3, 2010, and September 27, 2009, was \$3,000 and \$1.1 million, respectively. The exercise period for all stock options generally may not exceed 10 years from the date of grant. Stock option grants to individuals generally become exercisable over a service period of one to five years. There were no stock options granted in the three months ended October 3, 2010.

Performance Units and Nonvested Stock

The Company's LTIP provides for the issuance of performance units, which will be settled in stock subject to the achievement of the Company's financial goals. Settlement will be made pursuant to a range of opportunities relative to net earnings. No settlement will occur for results below the minimum threshold and additional shares shall be issued if the performance exceeds the targeted goals. The compensation cost of performance units is subject to adjustment based upon the attainability of the target goals.

Upon achievement of the performance goals, shares are awarded in the employee's name but are still subject to a two-year vesting condition. If employment is terminated (other than due to death or disability) prior to the vesting period, the shares are forfeited. Compensation expense is recognized over the performance period plus vesting period. The awards are treated as a liability award during the performance period and as an equity award once the performance targets are settled. Awards vest on the last day of the second year following the performance period.

A summary of the activity of the Company's nonvested shares during the three months ended October 3, 2010, is presented below:

	Number of Nonvested Shares	Weighted-Average Grant Price
Nonvested shares at June 27, 2010	---	\$ ---
Issued	119,338	12.30
Vested	---	
Forfeited	---	
Nonvested shares at October 3, 2010	119,338	\$ 12.30

For the quarters ended October 3, 2010, and September 27, 2009, compensation expense related to the LTIP was \$353,000, and \$308,000, respectively.

LaBARGE, INC.

FORM 10-Q

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-looking Statements

This report contains forward-looking statements that relate to future events or our future financial performance. We have attempted to identify these statements by terminology including "believe," "anticipate," "plan," "expect," "estimate," "intend," "seek," "goal," "may," "will," "should," "can," "continue," or the negative of these terms or other comparable terms. These statements include statements about our market opportunity, our growth strategy, competition, expected activities, and the adequacy of our available cash resources. These statements may be found throughout the report, including in the section of this report entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations." Readers are cautioned that matters subject to forward-looking statements involve known and unknown risks and uncertainties, including those described in our most recent Annual Report on Form 10-K. These risks and uncertainties may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Accordingly, we can give no assurances that any of the events anticipated by the forward-looking statements will occur, or if any of them do, what impact they will have on our results of operations or financial condition. We expressly decline any obligation to publicly revise any forward-looking statements that have been made to reflect the occurrence of events after the date of this report.

Given these uncertainties, undue reliance should not be placed on such forward-looking statements. Unless otherwise required by law, the Company disclaims an obligation to update any such factors or to publicly announce the results of any revisions to any forward-looking statements contained herein to reflect future events or developments.

Overview

The Company designs, engineers and produces sophisticated electronic and electromechanical systems and devices, and complex interconnect systems on a contract basis for its customers. Engineering and manufacturing facilities are located in Arkansas, Missouri, Oklahoma, Pennsylvania, Texas and Wisconsin.

The Company employs approximately 1,590 people, including approximately 1,350 people who provide support for production activities (including assembly, testing and engineering) and approximately 240 people who provide administrative support.

The Company uses a fiscal year ending the Sunday closest to June 30. The fiscal quarter ended October 3, 2010, contained 14 weeks while the fiscal quarter ended September 27, 2009, contained 13 weeks.

The Company's customers conduct business in a variety of markets with significant revenues from customers in the defense, medical, aerospace, natural resources, industrial and other commercial markets. As a contract manufacturer, revenues are impacted primarily by the volume of shipments in the particular period.

The Company provides information about its end markets to demonstrate the diversity of its customer base, which the Company believes helps to reduce potential volatility in its revenue stream. However, the Company does not target customers in individual markets, but rather targets companies whose manufacturing requirements match the services and capabilities the Company provides. Within all end markets, gross profit margins vary widely by customer and by contract.

The most significant factors influencing profitability in a particular period are: the mix of contracts with deliveries in that period and the volume of sales in relation to the Company's fixed costs during that period. Delivery schedules are generally determined by the Company's customers. The significant factors that influence the profitability of the individual contracts include: (i) the competitive environment in which the contract was bid; (ii) the experience level of the Company in manufacturing the particular product(s); (iii) the stability of the design of the product(s); and (iv) the accuracy of the Company's original cost estimates as reflected in the sale price for the product(s).

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The Company has a centralized sales organization. Though the selling and marketing personnel have a customer and prospective customer focus, they are not limited to exclusively developing a specific end market.

Results of Operations – Three Months Ended October 3, 2010

Backlog

(in thousands)

Change	October 3, 2010	June 27, 2010
Defense \$25,322	\$ 135,752	\$ 110,430
Natural resources 3,592	39,949	36,357
Industrial (2,273)	26,358	28,631
Medical 872	19,037	18,165
Commercial aerospace 367	1,979	1,612
Other 269	3,801	3,532
Total backlog \$28,149	\$ 226,876	\$ 198,727

The backlog at October 3, 2010, increased \$28.1 million from June 27, 2010. The \$25.0 million increase in defense backlog is primarily attributed to several large contracts related to producing interconnect and electronic assemblies for a variety of defense applications, including military aircraft, missile systems, radar systems and shipboard programs. The \$3.6 million increase in natural resources backlog is primarily comprised of bookings from wind power generation and oil-and-gas customers. The \$2.2 million decrease in industrial backlog is primarily attributed to a decrease in bookings of electronic and electromechanical assemblies used in capital equipment for glass container fabrication systems.

Approximately \$48.9 million of the backlog at October 3, 2010, is scheduled to ship beyond the next 12 months, pursuant to the shipment schedules of the contracts that comprise backlog. This compares with \$30.4 million at June 27, 2010.

Net Sales

(in thousands)

Change	October 3, 2010	September 27, 2009
Defense (294)	\$ 30,563	\$ 30,857
Industrial 1,644	22,624	10,980
Natural resources 1,352	21,291	9,939
Medical 512	7,364	6,852
Commercial aerospace (682)	1,185	1,867
Other (239)	2,421	2,660
Total net sales \$22,293	\$ 85,448	\$ 63,155

For the three months ended October 3, 2010, sales increased \$22.3 million, versus the comparable period a year earlier. Sales to industrial customers increased \$11.6 million primarily due to higher demand for capital equipment used in glass container fabrication systems and higher demand for electronic assemblies used in high-performance semiconductor test equipment. Sales to natural resources customers increased \$11.3 million primarily attributed to an increase in sales to wind power generation and oil-and-gas customers.

Sales to the Company's 10 largest customers represented 62% of total revenue for the three months ended October 3, 2010, versus 60% for the

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same period in fiscal 2010. The Company's top three customers for the three months ended October 3, 2010, were Owens-Illinois, Inc., 15.6%; American Superconductor, 10.1 %; and Schlumberger, Ltd., 9.0%. The Company's top three customers for the fiscal quarter ended September 27, 2009, were Owens-Illinois Inc., 10.9%; BAE Systems, 9.2%; and Raytheon Company, 8.6%.

Cost of Sales and Gross Profit

(dollars in thousands)

	Change	Three Months Ended	
		October 3, 2010	September 27, 2009
Cost of sales	\$ 17,092	\$ 68,017	\$ 50,925
Percent of net sales	(100) basis pts.	79.6%	80.6%
Gross profit	\$ 5,201	17,431	\$ 12,230
Gross profit margin	100 basis pts.	20.4%	19.4%

Gross profit margins vary significantly by contract. The most significant factors influencing profitability in a particular period are: the mix of contracts with deliveries in that period and the volume of sales in relation to the Company's fixed costs during the period. Delivery schedules are generally determined by the Company's customers. The significant factors that influence the profitability of individual contracts include: (i) the competitive environment in which the contract was bid; (ii) the experience level of the Company in manufacturing the particular product(s); (iii) the stability of the design of the product(s); and (iv) the accuracy of the Company's original cost estimates.

Cost of sales for the three months ended October 3, 2010, increased \$17.1 million, compared with the prior fiscal year, driven by the \$22.3 million increase in sales. Gross profit for the three months ended October 3, 2010, increased \$5.2 million, and gross profit margin increased 100 basis points versus the same period in the prior fiscal year. The increase in gross profit margin from 19.4% in the three months ended September 27, 2009, to 20.4% in three months ended October 3, 2010, was primarily driven by the fact that sales grew by 35.3% while indirect manufacturing costs grew only 10.7%, compared with the same period a year earlier. This was offset, in part, by a positive impact of \$227,000 or 40 basis points, for the payment of a claim on a contract completed in the third quarter of fiscal year 2009.

Selling and Administrative Expense

(dollars in thousands)

	Change	Three Months Ended	
		October 3, 2010	September 27, 2009
Selling and administrative expense	\$ 1,311	\$ 9,401	\$ 8,090
Percent of net sales) basis (180pts.	11.0%	12.8%

Selling and administrative expense increased by \$1.3 million for the three months ended October 3, 2010, compared with the three months ended September 27, 2009. The increase in expenses is primarily attributable to an increase in salaries and fringe benefit expense of \$1.2 million, versus the prior year period. Salaries increased \$711,000 in the quarter ended October 3, 2010, when compared with the quarter ended September 27, 2009. In addition, during the first quarter of fiscal 2011, the Company reinstated the employee stock purchase plan and the 401(k) match for its employees, which were suspended during the first quarter of fiscal year 2010. This resulted in additional compensation expense of \$100,000 for the quarter ended October 3, 2010, versus the year-ago period. Incentive salary expense also increased \$144,000, payroll taxes increased \$97,000, and other fringes increased \$161,000 in the first quarter ended October 3, 2010, when compared with the year-ago period.

Interest Expense

(in thousands)

Change	Three Months Ended	
	October 3, 2010	September 27, 2009
\$(110)	\$ 398	\$ 508

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Interest
expense

Interest expense decreased by \$110,000 for the three months ended October 3, 2010, versus the same period last year due to lower average debt levels.

Income Tax Expense

(in thousands)

		Three Months Ended	
Change	October 3, 2010	September 27, 2009	
Income tax expense	\$ 2,205	\$ 2,710	\$ 505

The estimated annual effective income tax rate for the three months ended October 3, 2010, was 35.8%, compared with 36.6% for the three months ended September 27, 2009. The income tax expense recorded for the three months ended September 27, 2009, was impacted favorably by \$795,000 for the recording of refunds due to a correction to the apportionment factor for state income tax returns as described in Note 1 of the Consolidated Financial Statements.

The Company was notified by the Internal Revenue Service ("IRS") in October 2010 that the IRS was conducting an examination of the fiscal year 2009 tax return. This examination is limited to transactions related to a controlled foreign corporation from which the Company purchases insurance.

Liquidity and Capital Resources

Cash Flow

(in thousands)

	Three Months Ended	
	October 3, 2010	September 27, 2009
Net cash provided by operating activities	\$ 3,037	\$ 6,262
Net cash used by investing activities	(558)	(2,196)
Net cash used by financing activities	(4,545)	(571)
Net (decrease) increase in cash and cash equivalents	\$ (2,066)	\$ 3,495

The Company's operations generated \$3.0 million of cash in the three months ended October 3, 2010, compared with cash generated of \$6.3 million in the three months ended September 27, 2009. The primary driver of the lower net operating cash flow in the fiscal 2011 first quarter, versus the same period a year earlier, was a \$24.3 million increase in cash disbursements for inventory purchases and other costs of operations. The higher inventory purchases and other operation costs were primarily driven by the increase in sales volume for the three months ended October 3, 2010, compared with the three months ended September 27, 2009. In addition, the cash used for payroll-related expenditures increased by \$7.1 million in the fiscal 2011 first quarter, compared with the fiscal 2010 first quarter, due to bonus payments made during the quarter ended October 3, 2010, and the timing of the payroll disbursements, which resulted in an additional payroll disbursement in the three months ended October 3, 2010, as compared with the three months ended September 27, 2009. These increased disbursements were offset by \$27.9 million of increased cash received from customers due to the higher sales levels.

The \$1.6 million decrease in cash used by the Company's investing activities in the three months ended October 3, 2010, versus the three months ended September 27, 2009, was primarily driven by a reduction of \$1.5 million in capital expenditures for equipment and facilities.

Stock Options

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The \$4.0 million increase in cash used by financing activities in the three months ended October 3, 2010, versus the three months ended September 27, 2009, is due to the fact that in the fiscal 2011 first quarter, the Company repaid long-term debt of \$4.5 million, compared with payments of \$40,000 in the fiscal 2010 first quarter. This was partially offset by short-term borrowings of \$550,000 during the three months ended October 3, 2010. The Company did not borrow any cash under its revolving credit facility during the quarter ended September 27, 2009.

Capital Structure

The Company entered into a senior secured loan agreement on December 22, 2008, amended on January 30, 2009. The following is a summary of certain provisions of the agreement:

- The agreement provides for a revolving credit facility, of up to \$30.0 million, which is available for direct borrowings or letters of credit. The facility is based on a borrowing base formula equal to the sum of 85% of eligible receivables and 35% of eligible inventories. As of October 3, 2010, \$550,000 was outstanding under the revolving credit facility. As of October 3, 2010, letters of credit issued were \$1.2 million, leaving an aggregate of up to \$28.2 million available under the revolving credit facility. This credit facility matures on December 22, 2011.
- The agreement provides for an aggregate \$45.0 million term loan, with quarterly principal payments beginning in September 2009 of \$2.0 million, increasing to \$2.5 million in September 2010 and increasing to \$2.7 million in September 2011. The balance is due on December 22, 2011.
- Interest on the revolving facility and the term loan is calculated at a base rate or LIBOR plus a stated spread based on certain ratios. For the fiscal quarter ended October 3, 2010, the average rate was approximately 3.61%.
- All loans are secured by substantially all the assets of the Company other than real estate.
- The Company must comply with covenants and certain financial performance criteria consisting of Earnings Before Interest, Taxes, Depreciation and Amortization ("EBITDA") in relation to debt, minimum net worth and operating cash flow in relation to fixed charges. The Company was in compliance with its borrowing agreement covenants as of and during the fiscal quarter ended October 3, 2010.

Interest Rate Swap:

To mitigate the risk associated with interest rate volatility, the Company entered into an interest rate swap agreement. This pay-fixed, receive-floating rate swap limits the Company's exposure to interest rate variability and allows for better cash flow control. The swap is not used for speculative purposes.

Under the original agreement, the Company fixed the interest payments to a base rate of 1.89% plus a stated spread based on certain ratios. The beginning notional amount is \$35.0 million, which will amortize simultaneously with the term loan schedule in the associated loan agreement and will mature on December 22, 2011. At October 3, 2010, the outstanding balance under the associated loan agreement was \$25.3 million.

On September 30, 2009, the Company made an additional payment in conjunction with the first principal payment under the loan agreement dated December 22, 2008. This additional payment, reflected in the financial statements as a current maturity of long-term debt in addition to the contractual payments due within the next twelve months, required a restructuring of the interest rate swap agreement. As a result, the fixed base rate under the revised agreement increased to 1.92%. This rate will apply until the swap matures on December 22, 2011.

The interest rate swap agreement has been designated as a cash flow hedging instrument, and the Company has formally documented, designated and assessed the effectiveness of the interest rate swap. The financial statement impact of ineffectiveness for the three months ended October 3, 2010, and September 27, 2009, was immaterial.

Fair Value:

The Company considered the carrying amounts of cash and cash equivalents, securities and other current assets and liabilities, including accounts receivable and accounts payable, to approximate fair value because of the short maturity of these financial instruments.

The Company has considered amounts outstanding under the long-term debt agreements and determined that carrying amounts recorded in the financial statements are consistent with the estimated fair value as of October 3, 2010.

Additionally, the interest rate swap agreement, further described above, has been recorded by the Company based on the estimated fair value as

Stock Options

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of October 3, 2010.

At October 3, 2010, the Company recorded a liability of \$390,000 classified within other long-term liabilities in the consolidated balance sheet, and accumulated other comprehensive loss of \$250,000 (net of deferred income tax effects of \$140,000) relating to the fair value of the interest rate swap contract.

The Company has classified its financial assets and liabilities using a three-level hierarchy for disclosure of fair value measurements, based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date, as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 – inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Company's interest rate swap is valued using a present value calculation based on an implied forward LIBOR curve (adjusted for the Company's credit risk) and is classified within Level 2 of the valuation hierarchy, as presented below:

(in thousands)

	Fair Value as of October 3, 2010			
	Level 1	Level 2	Level 3	Total
Other long-term liabilities:				
Interest rate swap derivative	\$ ---	\$ 390	\$ ---	\$ 390
	\$ ---	\$ 390	\$ ---	\$ 390

Other Long-Term Debt:

Other long-term debt includes capital lease agreements with outstanding balances totaling \$35,000 at October 3, 2010, and \$77,000 at June 27, 2010.

Maturities of Senior Long-Term Debt:

The aggregate maturities of long-term obligations are as follows:

(in thousands)

Fiscal Year	
2011	\$ 7,527
2012	25,258
Total	\$32,785

Stockholders' Equity and Debt

The following table shows LaBarge's equity and total debt positions:

(in thousands)

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	October 3, 2010	June 27, 2010
Stockholders' equity	\$ 120,598	\$ 115,640
Debt and capital lease obligations	33,335	37,327

The Company intends to renegotiate the senior loan agreement prior to its maturity in December 2011. Management believes the availability of funds going forward from cash generated from operations and available bank credit facilities should be sufficient to support the planned operations and capital expenditures of the Company's business for the next two fiscal years.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions in certain circumstances that affect amounts reported in the accompanying consolidated financial statements. In preparing these financial statements, management has made its best estimates and judgment of certain amounts included in the financial statements. The Company believes there is a likelihood that materially different amounts would be reported under different conditions or using different assumptions related to the accounting policies described below. Application of these accounting policies involves the exercise of judgment and use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates. The Company's senior management discusses the accounting policies described below with the Audit Committee of the Company's Board of Directors on a periodic basis.

The following discussion of critical accounting policies is intended to bring to the attention of readers those accounting policies that management believes are critical to the Company's consolidated financial statements and other financial disclosures. It is not intended to be a comprehensive list of all of the Company's significant accounting policies that are more fully described in the Notes to the Consolidated Financial Statements in the Annual Report on Form 10-K for the fiscal year ended June 27, 2010.

Revenue Recognition and Cost of Sales

The Company's revenue is derived from units and services delivered pursuant to contracts. The Company has a significant number of contracts for which revenue is accounted for under the percentage of completion method using the units of delivery as the measure of completion. This method is consistent with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 605-35 (formerly the Statement of Position 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts"). The percentage of total revenue recognized from contracts under the percentage of completion method is generally 35-55% of total revenue in any given quarter. These contracts are primarily fixed price contracts that vary widely in terms of size, length of performance period and expected gross profit margins. Under the units of delivery method, the Company recognizes revenue when title transfers, which is usually upon shipment of the product or completion of the service.

The Company also sells products under purchase agreements, supply contracts and purchase orders that are not within the scope of ASC Topic 605-35. The Company provides goods from continuing production over a period of time. The Company builds units to the customer specifications based on firm purchase orders from the customer. The purchase orders tend to be of a relatively short duration and customers place orders on a periodic basis. The pricing is generally fixed for some length of time and the quantities are based on individual purchase orders. Revenue is recognized in accordance with Staff Accounting Bulletin No. 104, "Revenue Recognition." Revenue is recognized on substantially all transactions when title transfers, which is usually upon shipment.

Therefore, revenue for contracts within the scope of ASC Topic 605-35 and for those not within the scope of ASC Topic 605-35 is recognized when title transfers, which is usually upon shipment or completion of the service.

However, the cost of sales recognized under both contract types is determined differently. The percentage-of-completion method for contracts that are within the scope of ASC Topic 605-35 gives effect to the most recent contract value and estimates of cost at completion. Contract costs generally include all direct costs, such as materials, direct labor, and subcontracts and indirect costs identifiable with or allocable to the contracts. Learning or start-up costs, including tooling and set-up costs incurred in connection with existing contracts, are charged to existing contracts. The contract costs do not include any sales, marketing or general and administrative costs. Revenue is calculated as the number of units shipped multiplied by the sales price per unit. The Company estimates the total revenue of the contract and the total contract costs and calculates the contract cost percentage and gross profit margin. The gross profit during a period is equal to the earned revenue for the period multiplied by the estimated contract gross profit margin. Thus, if no changes to estimates were made, the procedure results in every dollar of earned revenue having the same cost of earned revenue and gross profit percentage. This method is applied consistently on all of the contracts accounted for in accordance with ASC Topic 605-35.

The Company periodically reviews all estimates to complete as required by the authoritative guidance and the estimated total cost and expected gross profit are revised as required over the life of the contract. Any revisions to the estimated total cost are accounted for as a change of an estimate. A cumulative catch-up adjustment is recorded in the period of the change of the estimated costs to complete the contract. Therefore,

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cost of sales and gross profit in a period includes (a) a cumulative catch-up adjustment to reflect the adjustment of previously recognized profit associated with all prior period revenue recognized based on the current estimate of gross profit margin, as appropriate, and (b) an entry to record the current period costs of sales and related gross profit margin based on the current period sales multiplied by the current estimate of the gross profit margin on the contract. Cumulative adjustments are reported as a component of cost of sales.

For contracts accounted for using the percentage of completion method, management's estimates of material, labor and overhead costs on long-term contracts are critical to the Company. Due to the size, length of time and nature of many of our contracts, the estimation of costs through completion is complicated and subject to many variables. Total contract cost estimates are largely based on negotiated or estimated material costs, historical labor performance trends, business base and other economic projections. Factors that influence these estimates include inflationary trends, technical and schedule risk, performance trends, asset utilization, and anticipated labor rates.

The development of estimates of costs at completion involves procedures and personnel in all areas that provide financial or production information on the status of contracts. Estimates of each significant contract's value and estimate of costs at completion are reviewed and reassessed quarterly. Changes in these estimates result in recognition of cumulative adjustments to the contract profit in the period in which the change in estimate is made. When the current estimate of costs indicates a loss will be incurred on the contract, the total anticipated loss is recognized in that period.

Due to the significance of judgment in the estimation process described above, it is likely that different cost of sales amounts could be recorded if we used different assumptions, or if the underlying circumstances were to change. Changes in underlying assumptions, estimates, or circumstances may adversely or positively affect future financial performance.

In summary, the cumulative gross profit margin recognized through the end of the current period on a contract will equal the current estimate of the gross profit margin on the contract multiplied by the contract revenues recognized through the end of the current period. The current period gross profit will equal current period sales multiplied by the expected gross profit margin (on a percentage basis) on the contract plus or minus any net effect of cumulative adjustments to prior period sales under the contract.

In addition, when there is an anticipated loss on a contract, the entire loss is recorded in the period when the anticipated loss is determined. The loss is reported as a component of cost of sales. Therefore, the cumulative gross profit margin recognized through the end of the current period on a contract with an estimated loss will equal the current estimate of the gross profit margin on the contract multiplied by the contract revenues recognized through the end of the current period plus the provision for the additional loss on contract revenues yet to be recognized. The current period gross profit on a contract with a loss reserve will equal current period sales at a 0% gross profit margin plus or minus any net effect of cumulative adjustments to the loss reserve based on any changes to the estimated total loss on the contract.

This method of recording costs for contracts under ASC Topic 605-35 is equivalent to Alternative A as described in paragraph 35 of ASC Topic 605-35.

The contracts that are not subject to percentage of completion accounting are not subject to estimated costs of completion. Cost of sales under these contracts are based on the actual cost of material, labor and overhead charged to each job. The contract costs do not include any selling and administrative expenses. The Company generally performs the work under fixed price arrangements so the profit on the contract may be influenced by the accuracy of the estimates used at the time a particular job is bid, as reflected in the sales price for the product, including: material costs, inflation, labor costs (both hours and rates), complexity of the work, and asset utilization.

Inventories

Inventories, other than work-in-process inventoried costs relating to those contracts accounted for under percentage of completion accounting, are carried at the lower of cost or market value.

Inventoried costs relating to contracts accounted for under percentage of completion accounting are stated at the actual production cost, including overhead, tooling and other related non-recurring costs, incurred to date, reduced by the amounts identified with revenue recognized on units delivered. Selling and administrative expenses are not included in inventory costs. Inventoried costs related to these contracts are reduced, as appropriate, by charging any amounts in excess of estimated realizable value to cost of sales. The costs attributed to units delivered under these contracts are based on the estimated average cost of all units expected to be produced. This average cost utilizes, as appropriate, the learning curve concept, which anticipates a predictable decrease in unit costs as tasks and production techniques become more efficient through repetition. In accordance with industry practice, inventories include amounts relating to long-term contracts that will not be realized in one year. Since the inventory balance is dependent on the estimated cost at completion of a contract, inventory is impacted by all of the factors described in the Revenue Recognition and Cost of Sales section above. Inventoried costs related to those contracts not accounted for under percentage of completion accounting are carried at the lower of cost or market.

In addition, management regularly reviews all inventory for lower of cost or market value issues to determine whether any write-down to the lower of cost or market value is necessary. Various factors are considered in making this determination, including expected program life, recent sales history, predicted trends and market conditions. If actual demand or market conditions are less favorable than those projected by management, inventory write-downs may be required. For the quarters ended October 3, 2010, and September 27, 2009, expense for the

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write-down of inventory to lower of cost or market value charged to income before income taxes was \$472,000, and \$255,000, respectively.

Goodwill and Other Intangible Assets

The Company evaluates goodwill for impairment on an annual basis on the first day of June of each fiscal year, as well as whenever events or changes in circumstances during the fiscal year indicate that the carrying amount may not be recoverable. Potential impairment of goodwill is assessed by comparing the carrying value of the reporting unit to its estimated fair value. If the carrying value of the reporting unit exceeds its fair value, an impairment loss may be required to be recorded. The Company evaluates whether any triggering events have occurred during the fiscal year, such as a significant decrease in expected cash flows at a reporting unit or changes in market or other business conditions that may indicate a potential impairment of goodwill or other intangible assets. In addition, the Company monitors its market capitalization, compared with the carrying value of the Company.

The annual goodwill impairment testing is performed in accordance with FASB ASC Topic 350, Intangibles – Goodwill and Other (“ASC 350”). Under guidelines established by FASB ASC Topic 280, Segment Reporting (“ASC 280”) the Company operates as one operating segment. However, the goodwill impairment analysis is performed at a reporting unit level. A reporting unit is one level below an operating segment as defined by ASC 280. Goodwill is recorded on three of the Company’s reporting units. The goodwill was a result of purchase accounting during the acquisition of these reporting units.

The Company estimates the fair value of its reporting units based on a combination of a market approach and an income approach. The income approach utilizes the discounted cash flow model and the market approach is based on market data for a group of guideline companies. The Company also considers its market capitalization on the date of the impairment testing, compared with the sum of the fair values of all reporting units including those without goodwill recorded.

The discounted cash flow analysis requires the Company to make estimates and judgments about the future cash flows of each reporting unit. The future cash flow forecasts for each reporting unit are based on historical and forecasted revenue and operating costs. This, in turn, involves further estimates such as expected future revenue and expense growth rates, working capital needs at each reporting unit and future capital expenditures required to meet the revenue growth. The discount rate is based on the estimated weighted average cost of capital for each reporting unit, which considers the risk inherent in each reporting unit.

The Company performed its annual impairment test of goodwill as of June 1, 2010, and concluded that no impairment charges were required. Total goodwill is \$43.4 million. Based on the annual impairment test completed as of June 1, 2010, the Company determined that the fair value of two of the reporting units, which represented \$24.2 million of the total goodwill, was substantially in excess of the carrying value of the reporting units.

The remaining reporting unit, which was acquired in December 2008, had goodwill of \$19.2 million at June 1, 2010. The fair value of this reporting unit exceeded the carrying value of this unit by more than 20%. However, this is a relatively recent acquisition that was purchased prior to the economic slowdown and the disruptive events in the credit markets. The estimates and assumptions made in the Company’s estimate of the fair value of this reporting unit are inherently subject to significant uncertainties, many of which are beyond the control of the Company and there is no assurance that these results can be achieved. The primary assumptions for which there is a reasonable possibility of the occurrence of variation that would significantly affect the measurement value include the assumptions regarding discount rate utilized, revenue growth, expected operating profit margins, and working capital requirements.

The following is a summary analysis of the significant assumptions used by the Company to estimate the fair value of this reporting unit using the income approach and how the assumptions were developed:

Discount rate: The discount rate represents the expected return on capital and is based on the estimated weighted average cost of capital for the reporting unit. The discount rate used in determining the fair value of the reporting unit was 16%. This rate considers the risk inherent in the projections used to estimate the fair value of the reporting unit. This rate takes into account the uncertainty about the expected revenue growth of the reporting unit and expected operating margins as well as the past performance of the reporting unit. A change in the discount rate of 1% would indicate that the fair value of the reporting unit remains in excess of the carrying value of the unit. However, it would indicate that the excess of the fair value of the reporting unit over the carrying value of the reporting unit would be less than 20%.

Revenue growth assumptions: Projected annual growth assumptions are based on the Company’s and its peers historical operating performance adjusted for current and expected competitive and economic factors surrounding the electronic manufacturing services (“EMS”) industry. The long term expected growth rate for the EMS industry is seven percent. The Company expects sales growth rates for this reporting unit to exceed the long term industry average of seven percent during the next five years as the Company recovers from the economic slowdown in fiscal years 2009 and 2010. The growth rates will then normalize to industry rates and the Company used a terminal growth rate of 3% to calculate the terminal value in the discounted cash flow analysis. The Company expects the growth rates for the reporting unit to exceed the long-term growth rate of the EMS industry because (1) the Company expects that in fiscal year 2011, and fiscal year 2012, existing customers of the reporting unit

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will recover to their sales rates prior to the economic slowdown, and (2) the Company believes that with access to the Company's larger sales force and more competitive financial strength the reporting unit will be able to attract new customers and gain additional business from existing customers.

Operating profit margin assumptions: The forecasted operating profit used in the income approach for the reporting unit is expected to improve in the future years as a result of implementing lean efficiency improvements, leveraging of the Company-wide purchasing agreements and leveraging fixed costs.

Working Capital assumptions and capital expenditures: Working capital requirements were forecasted based on the reporting unit's historical performance and considering industry averages. Capital expenditures were forecasted based on current spending plans for the next two fiscal years and on industry averages, thereafter.

The Company also used the market approach to estimate the fair value of the reporting unit. The Company utilizes the guideline public company method in which valuation pricing multiples are derived from the market share prices of stocks of companies that are engaged in the same or similar lines of business as the reporting unit, and that are actively traded on a free and open market. The derived multiples are then applied to the reporting unit's financial metrics producing indications of value, which are correlated to reach a final indication of value. The Company used Earnings before Interest Depreciation and Amortization ("EBITDA") multiples based on the last 12 months and for the next 12 months to EBITDA to estimate fair value using a market approach. These multiples range from 5.0 to 7.0 times EBITDA. In addition, the Company included a control premium in this analysis. This resulted in a market value that was within 10% of the estimated fair value using the income approach.

The Company believes the market data used in the market approach and the estimated future cash flows and discount rate used in the income approach are reasonable; however, changes in estimates could materially affect the Company's estimates of the fair value of the reporting units and therefore, the results of the Company's impairment analysis. If the current economic conditions deteriorate, causing a decline in the Company's stock price or expected cash flows, impairments to one or more businesses could occur in future periods whether or not connected to the annual impairment analysis. Any related losses or required write-downs could have a material adverse effect on the Company's financial results.

Recently Adopted Accounting Standards

In June 2009, the FASB issued an accounting standards update included in ASC Topic 810, "Consolidation," which amends previous guidance to require an analysis to determine whether a variable interest gives a company a controlling financial interest in a variable interest entity. An ongoing reassessment of financial responsibility is required, including interests in entities formed prior to the effective date of this guidance. This guidance also eliminates the quantitative approach previously required for determining whether a company is the primary beneficiary. It is effective for fiscal years beginning after November 15, 2009. This guidance was adopted on June 28, 2010 and adoption did not have a material impact on the Company's consolidated financial statements.

In October 2009, the FASB issued guidance titled "Revenue Recognition – Multiple Deliverable Revenue Arrangements" (Accounting Standards Update 2009-13), which requires entities to allocate revenue in an arrangement using estimated selling prices of the delivered goods and services based on a selling price hierarchy. The guidance eliminates the residual method of revenue allocation and requires revenue to be allocated using the relative selling price method. This guidance should be applied on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. This guidance was adopted by the Company on June 28, 2010, and adoption did not have a material impact on the Company's consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Foreign Currency Risk

The Company has no sales offices or facilities outside of the United States. Sales for exports were 10.9% of total sales in the fiscal quarter ended October 3, 2010, and less than 10% of total Company revenue for the fiscal quarter ended September 27, 2009. Export sales exceeded 10% of total revenue due to a large contract related to wind power generation equipment. This contract is denominated in U.S. dollars and, therefore, the Company does not have foreign currency risk associated with the related accounts receivable.

Interest Rate Risk

As of October 3, 2010, the Company had \$33.3 million in total debt. Of the total debt, \$25.3 million has a fixed rate through an interest rate swap agreement, and therefore, is not subject to interest rate risk. Another \$284,000 is subject to a fixed interest rate through borrowing agreements and is not subject to interest rate risk. The interest rate on the remaining \$7.8 million is subject to fluctuation. If interest rates increased 1%, the additional interest cost to the Company would be approximately \$69,000 for one year.

Item 4. Controls and Procedures.

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Evaluation Of Disclosure Controls And Procedures

Management, under the supervision and with the participation of the Company's Chief Executive Officer and President, and the Company's Vice President and Chief Financial Officer, reviewed and evaluated the effectiveness of the Company's disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report.

Based on such review and evaluation, the Company's Chief Executive Officer and President and Vice President and Chief Financial Officer concluded that, as of the end of the period covered by this report, the disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934, as amended, (i) is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and (ii) is accumulated and communicated to the Company's management, including its Chief Executive Officer and President and Vice President and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes In Internal Controls

During the three months ended October 3, 2010, there were no changes in internal control over financial reporting identified in connection with management's evaluation that have materially affected or that are reasonably likely to materially affect the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1A. Risk Factors.

Our Annual Report on Form 10-K for the year ended June 27, 2010, includes "Risk Factors" under Item 1A of Part I. There have been no material changes from the risk factors described in our Form 10-K. The information should be read in conjunction with, the risk factors and information disclosed in our Form 10-K.

Item 6. Exhibits.

- | | |
|------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 31.1 | Certification by Chief Executive Officer pursuant to Exchange Act Rule 13a-14 and 15d-14, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification by Chief Financial Officer pursuant to Exchange Act Rule 13a-14 and 15d-14, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification by Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

LaBarge, Inc.

Date: November 4, 2010

By: /S/ DONALD H. NONNENKAMP

Name: Donald H. Nonnenkamp
Vice President and Chief Financial Officer

